

Message Text

LIMITED OFFICIAL USE

PAGE 01 BUENOS 06998 241349Z

46

ACTION ARA-20

INFO OCT-01 ISO-00 AID-20 CIAE-00 COME-00 EB-11 FRB-02

INR-10 NSAE-00 RSC-01 TRSE-00 XMB-07 OPIC-12 SPC-03

CIEP-02 LAB-06 SIL-01 OMB-01 FTC-01 L-03 H-03 AGR-20

PRS-01 PA-03 USIA-15 DRC-01 /144 W

----- 045574

R 241210Z SEP 73

FM AMEMBASSY BUENOS AIRES

TO SECSTATE WASHDC 3690

LIMITED OFFICIAL USE BUENOS AIRES 6998

E.O. 11652: N/A

TAGS: EIND, AR

SUBJ: ARGENTINE SUPREME COURT DECISION AGAINST PARKE DAVIS

REF: STATE 182168

1. SUMMARY: SUPREME COURT DECISION AGAINST PARKE DAVIS ARGENTINA IS CULMINATION LENGTHY COURT CASE IN WHICH PARKE DAVIS CHALLENGED TAX BUREAU POSITION ON ROYALTY PAYMENTS BY SUBSIDIARY TO CONTROLLING PARENT COMPANY. LOCAL PRESS HAS LINKED THIS DECISION, SWIFT DELTEC DECISION, AND PROPOSED FOREIGN INVESTMENT LAW AS MAJOR INITIATIVES OF NEW GOVERNMENT AGAINST MULTINATIONAL COMPANIES, BUT IN FACT SUPREME COURT FINDINGS ONLY CONFIRM 1970 AND 1971 DECISIONS OF LOWER COURTS AND WERE NOT UNEXPECTED BY BUSINESS COMMUNITY. WHILE FULL IMPLICATIONS DECISION STILL UNKNOWN, MAJOR IMMEDIATE EFFECT ON US AND OTHER FOREIGN SUBSIDIARIES COULD BE SIZEABLE CLAIMS FOR BACK TAXES. END SUMMARY.

2. ARGENTINE GENERAL TAX BUREAU HAS TAKEN POSITION, AT LEAST IN RECENT YEARS, THAT PAYMENTS OF ROYALTIES, TECHNICAL SERVICE FEES, AND INTEREST BY A LOCAL BRANCH OR SUBSIDIARY TO A FOREIGN CORPORATION SUBSTANTIALLY CONTROLLING OR FULLY OWNING THE LOCAL

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 02 BUENOS 06998 241349Z

SUBSIDIARY ARE IN FACT REMITTANCES OF PROFIT RATHER THAN NECESSARY

COSTS OF OPERATION, AND THEREFORE ARE NOT DEDUCTIBLE FROM GROSS INCOME IN ESTABLISHING TAX BASE OF SUBSIDIARY. UNDER CURRENT TAX LAW, EFFECTIVE RATE OF TAX ON THESE PAYMENTS WHEN REMITTED ABROAD ROUGHLY EIGHT PERCENT BELOW RATE ON PROFITS OR DIVIDENDS REMITTED ABROAD. NO CORRESPONDING DIFFERENCE EXISTS IN TAX RATES ON SUCH PAYMENTS MADE TO LOCAL RESIDENTS.

3. PARKE DAVIS ARGENTINA AND SUBSIDIARIES OTHER FOREIGN FIRMS CONTESTED TAX BUREAU POSITION IN COURTS. PARKE DAVIS CASE WAS FIRST TO REACH SUPREME COURT, WHICH CONFIRMED ON JULY 31 FINDINGS OF LOWER COURTS, I.E., NATIONAL TAX COURT ON MARCH 14, 1970 AND COURT OF APPEALS ON AUG 31, 1971, UPHOLDING POSITION OF TAX BUREAU.

4. TAX BUREAU'S ORIGINAL RULING THIS CASE, ISSUED IN 1968 HELD THAT FOR PURPOSE OF DETERMINING TAX BASE OF PARKE DAVIS ARGENTINA FROM 1962 FORWARD, ROYALTY PAYMENTS TO PARENT FIRM SHOULD HAVE BEEN CONSIDERED REMITTANCES OF PROFITS RATHER THAN ROYALTY PAYMENTS. THIS AND SUBSEQUENT COURT DECISIONS, BASED ON FACT THAT PARENT FIRM, PARKE DAVIS OF DETROIT, OWNED 99.95 PERCENT OF ASSIGNED CAPITAL OF LOCAL FIRM. (PARDVOO, INC. OF DETROIT SHOWN AS OWNER OF MOST OF REMAINING SHARES, WHILE ONLY ABOUT .002 PERCENT OF SHARES HELD BY RESIDENTS OF ARGENTINA.)

5. SUPREME COURT DECISION DREW ON ABOVE AND ALSO (A) REFERRED TO ARTICLE IN ARGENTINE INCOME TAX LAW PROHIBITING DEDUCTIONS, AS COSTS, OF ANY INCOME DRIVED FROM INVESTMENT IN COMPANY BY PARTNERS, (B) CITED ESTABLISHED PROCEDURE UNDER TAX LAW BY WHICH INTERPRETATION OF LAW AND TAXABLE FACTS TO BE BASED ON ECONOMIC REALITY (REALIDAD ECONOMICA) RATHER THAN LEGAL FORM OF ORGANIZATION, (C) EXPRESS COURT'S VIEW THAT NO LICENSE AGREEMENT ACTUALLY EXISTS SINCE LOCAL FIRM LACKED NECESSARY INDEPENDENCE FROM PARENT COMPANY TO ENTER INTO VALID CONTRACT WITH LATTER, AND (D) DENIED THAT TAX LAW PERMITS PARENT COMPANY TO DECIDE HOW IT WILL RECEIVE INCOME FROM ITS INVESTMENTS, TO EXTEND THAT SPLITTING INCOME BETWEEN PROFITS AN ROYALTIES REDUCES TAX PAYMENTS IN ARGENTINA. TEXT OF SUPREME COURT DECISION AND COMMENT ON CASE, IN ENGLISH, RECENTLY PUBLISHED IN US LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 03 BUENOS 06998 241349Z

CHAMBER OF COMMERCE MAGAZINE BEING POUCHED.

6. LOCAL PRESS HAS LINKED THIS DECISION WITH SWIFT-DELTEC DECISION AND PROPOSED FOREIGN INVESTMENT LAW AS EXAMPLES OF NEW GOVERNMENT'S INITIATIVES AGAINST MULTINATIONAL CORPORATIONS. WHILE POLITICAL VIEWS OF NEWLY APPOINTED SUPREME COURT MAY HAVE AFFECTED SOME ASPECTS ITS DECISION, BASIC POINTS ARE NOT NEW WITH THIS COURT. IN PARTICULAR, CONCEPT OF LOOKING BEHIND

LEGAL STRUCTURE TO DETERMINE "ECONOMIC REALITY" APPEARS TO BE ESTABLISHED PROCEDURE IN ARGENTINE TAX LAW AND WAS CITED IN EARLIER DECISIONS ON CASE BY BOTH LOWER COURTS. ON THE OTHER HAND, THE EXTENSION OF THIS CONCEPT TO CASES OUTSIDE OF THE TAX FIELD, I.E., THE SWIFT-DELTEC CASE, DOES APPEAR TO BE A DEPARTURE FROM PREVIOUS PRACTICE.

7. IMPLICATION OF PARKE DAVIS DECISION ON OTHER SIMILAR CASES PENDING BEFORE TAX BUREAU AND COURTS STILL BEING ASSESSED BY COMPANIES AND THEIR ATTORNEYS. SOME SOURCES HAVE INDICATED THAT FAILURE OF PARKE DAVIS TO ATTEMPT TO ESTABLISH THAT THERE WAS AN ACTUAL TRANSFER OF TECHNOLOGY IN INITIAL PRESENTATION TO TAX COURT MAY HAVE CONTRIBUTED TO SUBSEQUENT UNFAVORABLE DECISIONS. PRECEDENT THUS CREATED HOWEVER WILL NOW ADVERSELY AFFECT EVEN THOSE CASES IN WHICH TECHNOLOGY TRANSFER CAN BE ESTABLISHED. AS YET, WE HAVE RECEIVED NO COMPLAINTS, HOWEVER THAT COURT'S DECISION WAS IMPROPER OR POLITICALLY MOTIVATED.

8. IMPORTANT POINTS STILL TO BE CLARIFIED INCLUDE: (A) DEGREE OF OWNERSHIP BY PARENT FIRM WHICH WILL BE CONSIDERED BY TAX BUREAU AND/OR COURTS TO CONSTITUTE CONTROL AND IDENTITY OF INTEREST WITH LOCAL FIRM. WE HAVE HEARD ESTIMATES RANGING FROM 50 TO 80 PERCENT. (B) EXTENSION OF DECISION TO APPLY ALSO TO PAYMENTS OF INTEREST AND TECHNICAL SERVICE FEES. THIS SEEMS LIKELY, AND WE UNDERSTAND THAT IN MANY CASES, INTEREST PAYMENTS TO PARENT COMPANY MAY HAVE BEEN SUBSTANTIALLY GREATER THAN ROYALTIES. (C) EXTEND TO WHICH TAX BUREAU WILL REQUIRE PAYMENT OF BACK TAXES. STATUTE OF LIMITATIONS WOULD APPARENTLY PERMIT CLAIMS TO EXTEND BACK FOR 5 YEARS. (D) EXTEND TO WHICH RECENTLY APPROVED LAW INTENDED TO ENCOURAGE GENERAL PAYMENT OF BACK TAXES BY REDUCING LIABILITY WILL APPLY TO SPECIAL CASES OF THIS TYPE.

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 04 BUENOS 06998 241349Z

9. GOVERNMENT'S POSITION ON ABOVE POINTS STILL NOT CLEAR. IN THIS REGARD, ONE OF DIFFERENCES PURPORTEDLY HOLDING UP CONGRESSIONAL APPROVAL OF FOREIGN INVESTMENT LAW IS CHAMBER OF DEPUTIES UNWILLINGNESS TO ACCEPT SENATE AMENDMENT WHICH WOULD CODIFY SUBSTANCE OF PARKE DAVIS DECISION.
LODGE

LIMITED OFFICIAL USE

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: LITIGATION, DRUGS, FOREIGN INVESTMENTS, TAXES, DEBTS
Control Number: n/a
Copy: SINGLE
Draft Date: 24 SEP 1973
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: collinp0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1973BUENOS06998
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: n/a
From: BUENOS AIRES
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1973/newtext/t19730916/aaaaalht.tel
Line Count: 160
Locator: TEXT ON-LINE
Office: ACTION ARA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: STATE 182168
Review Action: RELEASED, APPROVED
Review Authority: collinp0
Review Comment: n/a
Review Content Flags:
Review Date: 15 JAN 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <15-Jan-2002 by martinjw>; APPROVED <04 MAR 2002 by collinp0>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: ARGENTINE SUPREME COURT DECISION AGAINST PARKE DAVIS
TAGS: EIND, AR, PARKE DAVIS
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005